

STATE OF MICHIGAN
IN THE SUPREME COURT

Appeal from the Michigan Court of Appeals
Michael J. Talbot, Peter D. O'Connell, and Donald S. Owens

On Appeal from the Michigan Tax Tribunal
Tribunal Judge Preeti P. Gadola

HARMONY MONTESSORI CENTER,
Petitioner/Appellant

Supreme Court Docket No. 154819

Court of Appeals No. 326870

v

MTT Docket No. 370214

CITY OF OAK PARK
Respondent/Appellee.

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**PETITIONER HARMONY MONTESSORI CENTER'S
REPLY BRIEF IN SUPPORT OF APPLICATION FOR LEAVE TO APPEAL**

ORAL ARGUMENT REQUESTED

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INTRODUCTION

As Harmony explained in its *Application for Leave*, the results of this case present two issues that require this Court's attention. First, this case presents an issue of first impression for this Court involving the scope and applicability of the Court of Appeal's decision in *David Walcott Kendall Memorial School v City of Grand Rapids*, 11 Mich App 231; 160 NW2d 778 (1968) in the pre-primary setting. Although the *Walcott* decision provides some guidance for the Tribunal and courts to determine whether an educational institution should receive an *ad valorem* property tax exemption under MCL 211.7n, *Walcott*'s "would" and "could" test for determining the relief of government burden is vague in how it would apply to different kinds of educational institutions. The foremost example of this is the Tribunal's application of the *Walcott* factors in two cases involving Montessori pre-primary and primary educational institutions that resulted in completely different conclusions.

The current case involves a significant difference in opinion as to the objective or subjective factors that should be used to evaluate educational institutions under *Walcott* for tax exemption under MCL 211.7n. The Tribunal, for instance, looked at the parents' willingness to pay for education as a justification for granting the exemption in one case, but denying the exemption in another case. Compare *Petoskey Montessori Children's House v Bear Creek Twp*, 1986 WL 20565 (1986) with *Harmony Montessori Center v Oak Park*, unpublished per curiam opinion of the Court of Appeals, issued October 13, 2016 (Docket No. 326870). Comparing each outcome demonstrates a fundamental change in how the Tribunal applies *Walcott*.

Second, this case is guided by this Court's decision in *Wexford Medical Group v City of Cadillac*, 474 Mich 192; 713 NW2d 734 (2006), yet both the Tribunal and the Court of Appeals reached a contrary conclusion. Not only does this decision affect Petitioner, but it is detrimental to

Michigan's non-profit educational institutions. The Court of Appeals upholds the Tribunal's decision that a taxpayer must lose its charitable status under MCL 211.7o, if an organization makes the financial decision to raise costs for its services. See *Harmony Montessori Center v Oak Park*, unpub op at 8. However, this Court specifically stated in *Wexford* that if "the charges collected from patients were not larger than were necessary to the successful maintenance of the institution" that this Court would adopt an "untenable position," if the institution could not accept any fees. *Wexford*, 474 Mich at 206 (citing *Mich Sanitarium & Benevolent Ass'n v Battle Creek*, 138 Mich 676, 682-83; 101 NW 855 (1904)). A reasonable rule came to light in *Michigan Sanitarium* that "a corporation is sufficiently charitable to entitle it to the privileges of the act when the charges collected for services are not more than are needed for its successful maintenance." *Id.* (quoting 138 Mich at 683). If this Court allows the Tribunal and Court of Appeals' decisions to stand, it will advance the "untenable position" the *Wexford* Court warned of.

Accordingly, Petitioner respectfully requests that, for the reasons set forth in its *Application for Leave to Appeal and Reply*, this Court grant the Application and permit this taxpayer leave to appeal from the Court of Appeal's Opinion dated October 13, 2016. In the alternative, Petitioner respectfully requests that this Honorable Court reverse the Court of Appeal's decision and remand for the court to consider both an objective application of the Tribunal's prior precedent against the Petitioner's facts and perform a full inquiry of Petitioner's "overall charitable nature" as required by *Wexford*.

REPLY ARGUMENT

I. THE TAX TRIBUNAL ADOPTED A WRONG PRINCIPLE OF LAW WHEN IT IGNORED PUBLISHED TRIBUNAL PRECEDENT DIRECTLY APPLICABLE TO THE PRE-PRIMARY EDUCATIONAL SETTING.

Respondent incorrectly argues that Petitioner's reliance on *Petoskey Montessori Children's House v Bear Creek Twp*, 1986 WL 20565 (1986) is incorrect because it is "qualitatively and quantitatively distinguishable." First, the Tribunal's decision in *Petoskey* is published precedent¹ and established what students should be considered in determining whether an "institution is assuming a (sufficient) portion of the burden of educating the student which otherwise falls on tax-supported schools." *Petoskey*, 1986 WL 20565, at *3 (citing *Walcott*, 11 Mich App at 240). In *Petoskey*, the institution offered preschool and kindergarten programs for three years at issue, while offering elementary education for only **one** of the three years. *Id.* at *2 (emphasis added). The institution enrolled students in the following programs:

Tax Year	Total Number of Students	Students in Preschool	Students in Kindergarten	Students in Elementary
1979	29	22	7	-
1980	37	29	8	-
1981	46	22	13	11

Id.

¹ MCL 205.765 states "[a] decision of the division is not a precedent unless so designated by the tribunal." In *Petoskey*, the decision specifically states "IT IS HEREBY ORDERED that the final Opinion and Judgment in this cause shall be and hereby is declared precedential." *Petoskey*, 1986 WL 20565, at *1.

Petitioner enrolled students at the following program levels:

School Year	Total Number of Students	Students in Preschool*	Students in Kindergarten	Students in Elementary
2008-2009	27	23	4	-
2009-2010	26	22	4	-
2010-2011	26	20	6	-
2011-2012	28	20	8	-
*Students participating in Preschool and Kindergarten programs are placed into the "Students in Kindergarten" category.				

See JSOF, ¶ 23.

If this Court placed Petitioner and the educational institution in *Petoskey* side-by-side, the Montessori-school in question offers the same educational programs, teaching methods, tuition for services, and has a similar class-size proportionality. Failing to include preschool students in Petitioner's case prevents it from showing "the institution is assuming a (sufficient) portion of the burden of educating the student which otherwise falls on tax-supported schools." *Petoskey*, 1986 WL 20565, at *3 (citing *Walcott*, 11 Mich App at 240). Respondent relies on the word "substantial" requiring some form of numerical analysis when evaluating a substantial portion of the total students. This Court must provide direction on how programs are analyzed for the "substantial" analysis in light of the Tribunal's deviation from its own precedent in *Petoskey*.

A key difference between the educational institution involved in *Walcott* and the instant case is that *Walcott* involved post-secondary education by a specialized trade school, whereas this case involves pre-primary education. The pre-primary skills taught are a necessary prerequisite to students progressing in elementary school grades. Respondent ignores the fact that the skills taught at the Montessori schools in both *Harmony* and *Petoskey* cases are the same foundational skills required for successful completion of elementary school that follows. If

students arrive to a public school without these foundational skills, the student would not be able to advance in elementary school until the state school teaches them those skills. This is a significant consideration in the government's burden that was not addressed by the courts.

Respondent puts particular emphasis on Petitioner's failure to produce testimony from former parents stating where their children attended school post-Petitioner or where their children would attend if Petitioner were not in existence. The logic and inference made by Respondent by relying on *Petoskey* is unfounded. The *Petoskey* tribunal specifically addresses the parents' involvement in the education process:

The fact that the parents of the Montessori School children are willing to pay the tuition costs and the fact that these parents are actively involved in the educational process itself (per testimony) indicate to us that they are concerned with their children's education. Therefore, if the Montessori [sic] School did not exist, we are persuaded that a high percentage of these children would attend the comparable classes offered by their local school district.

Petoskey, 1986 WL 20565, at *3. In Petitioner's case, the Tribunal stated "given that the Montessori Method is a specify type of teaching . . . if [Petitioner] didn't exist, the parents of [Petitioner] students would send them to another Montessori school, but not to public school." *Harmony Montessori Center v City of Oak Park*, unpublished opinion of the Michigan Tax Tribunal, issued March 20, 2015 p 5 (Docket No. 370214). Beyond the fact that this reasoning conflicts with its holding in the *Petoskey* case, it is not supported by the evidence. Given the significant fundamental differences in decisions among similarly situated early childhood Montessori programs, it is evident that this Court's guidance is required to provide direction for the future of pre-primary educational institutions seeking a property tax exemption under MCL 211.7n. Further evidence for granting Petitioner's *Application* is that both the Petitioner and Respondent rely on the same case law, yet reach opposite results.

Respondent incorrectly ignores most of the *Walcott* factors and looks primarily at the number of students who would attend a state-funded school if petitioner were not in existence. *Response to Application*, p 32. The *Walcott* court suggested factors such as admission, student qualifications, field of student study, amount of time to complete study, and the quality and quantity of courses offered. *Walcott*, 11 Mich App at 240; 160 NW2d at 782. Respondent's myopic analysis guts the spirit and intention of the varied *Walcott* factors. Many of these factors do not comprehend a pre-primary program.

The Tribunal and Court of Appeals focus on the factor related to "comparative quality and quantity" of education is not supported by the *Walcott* court. *Walcott* involved a specialized post-secondary art school and compared its programs to that of Michigan State University and other post-secondary institutions. It is logical that a small specialized school and a large public university would not provide the same teaching environment, but would provide similar skills throughout each program. This is the meaning of the "comparative quality and quantity" of the education offered. The Tribunal and Court of Appeals' reasoning focused on the Montessori-teaching method compared to state-funded programs adopts a wrong principle of law, when it comes to evaluating whether a substantial number of students would attend a state-funded school. The *Walcott* court appreciated and understood the developing educational environment in that "[i]t is apparent that the rapidly changing concept of mass education has required a proliferation of new institutions . . . to provide for the increasing desire and needs." 11 Mich App at 238; 160 NW2d at 781. Petitioner asserts that looking at factors such as quality and necessity of skills is an important factor that follows from *Walcott*. The *Walcott* court realized the skills taught by an institution are essential in evaluating an educational institution. This is actually confirmed in *Michigan Laborers' Training & Apprenticeship Fund v Twp of Breiting*,

unpublished per curiam opinion of the Court of Appeals, issued October 23, 2012 (Docket No. 202723). In that case, petitioner failed to show that there were state supported programs whereby participants could become apprentices or journeymen. *Id.* at *3. Contrary to *Michigan Laborers*, Harmony provided uncontroverted evidence that the skills taught in its programs are directly applicable to state-funded preschool, kindergarten, and elementary school programs. If Petitioner were not in existence, the State would have the burden to teach the same mandatory, foundational skills to students.

Respondent focuses only on affirming the decisions of the Tribunal and the Court of Appeals, rather than addressing the grounds for the *Application* related to this argument. For these reasons, Petitioner requests this Court grant its *Application for Leave* in order to address the disparity among similar situated pre-primary schools and to address if the *Walcott* “would” and “could” test is directly applicable in the pre-primary educational environment.

II. THE TAX TRIBUNAL AND THE COURT OF APPEALS ADOPTED A WRONG PRINCIPLE OF LAW BY TAKING AN UNTENABLE POSITION RELATED TO SERVICE COST INCREASES AND PLACING AN ARTIFICIAL PARAMETER ON THE INSTITUTION’S BUSINESS DECISIONS.

Respondent contends that Petitioner “did not offer its services to anyone who walked in the door, but instead, limited its services to those who are able to pay.” *Response to Application*, p 41. This statement attempts to cast Petitioner’s services as discriminatory; however, the parties stipulated that “[i]n providing educational services . . . Petitioner, for the tax years in issue, did not discriminate among recipients of its services.” JSOF ¶ 11. The Tribunal and the two Court of Appeals’ panels dismissed Petitioner’s charitable status on the issue of “whether Harmony made up for operating losses by passing those losses onto those receiving its services.” *Response to Application*, p 41-42.

This Court, in *Wexford*, provided a thorough analysis for what should be considered when a charity makes a business decision to raise the cost for the services it charges. This Court understood the fact that non-profit charities do not have to choose between raising costs for services and losing its charitable property exemption. It reasoned that if a charitable institution received “charges collected from patients . . . not larger than were necessary to the successful maintenance of the institution,” this Court would adopt an “untenable position,” if the institution could not accept any fees. *Wexford*, 474 Mich at 206 (quoting *Mich Sanitarium*, 138 Mich at 682-83). A more sensible rule came to light in *Michigan Sanitarium* that “a corporation is sufficiently charitable to entitle it to the privileges of the act when the charges collected for services are not more than are needed for its successful maintenance.” *Id.* (quoting 138 Mich at 683). The parties stipulated that “Petitioner charged fees for participation in its programs; these fees did not exceed the amount Petitioner required to provide its services.” JSOF ¶ 12.

Petitioner’s tuition satisfies *Wexford* because it is not completely bore by its parents. In *Wexford*, the petitioner “sustain[ed] notable financial losses by not restricting the number of Medicare and Medicaid patients it accept[ed],” but bore “those losses rather than restricting its treatment of patients who cannot afford to pay.” 474 Mich at 216. The petitioner’s losses were “*not fully subsidized* by the patients, but by petitioner’s parent corporations, patients who can afford to pay, and to some extent, by government reimbursements.” *Id.* at 217 (emphasis added). Respondent admits in its *Response* exactly this same point: “[Petitioner] made up for losses, *at least in part*, by charging its families increased tuition in subsequent years.” *Response to Application*, p 42 (emphasis added). The Court of Appeals statement in its dissent is directly on point with this Court’s reasoning in *Wexford* that “[Petitioner] established that its costs are *not fully subsidized* by tuition. Instead, [Petitioner] also holds fundraisers and accepts donations.”

Harmony Montessori Center v Oak Park, unpublished opinion of the Court of Appeals, issued October 13, 2016 at p 2 (Docket No. 326870) (O'CONNELL, J., dissenting). Respondent's reasoning that increasing charges must negate a property tax exemption ignores the practical reality that non-profits must bear all costs of operations and that while a non-profit should not profit from its endeavors, sound financial planning dictates that a non-profit must be able to raise enough money through fundraising and charges to at least break-even. Respondent has not proffered evidence or case law that a non-profit must operate at a financial loss. It would also dictate an unworkable requirement that a non-profit would have to justify its cost increases each year to the tax assessor, who could make the decision that its increases in charges for a particular year were not allowed.

Respondent, the Tribunal, and Court of Appeals also emphasize that Petitioner never offered free tuition. *Wexford* directly negates this claim by stating "[t]he Legislature provided no measuring device with which to gauge an institution's charitable composition, and we cannot presuppose the existence of one." *Wexford*, 474 Mich at 213. "To say that an institution must devote a certain percentage of its time or resources to charity before it merits a tax exemption places an artificial parameter on the charitable institution statute that is unsanctioned by the Legislature." *Id.*


If this Court does not correct the untenable position adopted by the Tribunal and both Court of Appeals decisions, it could jeopardize most non-profit institutions' charitable property tax exemption, strictly based on the financial decision to offset costs or how it conducts its operations.

CONCLUSION AND RELIEF REQUESTED

Petitioner respectfully requests that, for the reasons set forth in its *Application for Leave to Appeal*, this Court should the *Application* and permit this taxpayer leave to appeal from the Court of Appeal's Opinion dated October 13, 2016. In the alternative, Petitioner respectfully requests that this Honorable Court reverse the Court of Appeal's decision and remand for the court to consider both an objective application of the tribunal's prior precedent against the Petitioner's facts and perform a full inquiry of Petitioner's "overall charitable nature" as required by *Wexford*.

Respectfully submitted,

Dated: January 30, 2017

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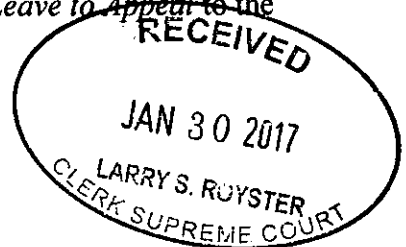
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PROOF OF SERVICE

Joshua Wease certifies that on the 30th day of January 2017, he served a copy of the *Petitioner-Appellant's Reply to Brief In Support of Application for Leave to Appeal to the Michigan Supreme Court* by first class mail to:

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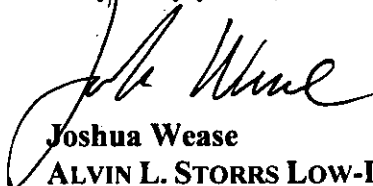
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***Re: Harmony Montessori Center v. City of Oak Park; Appellant's Reply Brief in
Support of Application for Leave to Appeal***

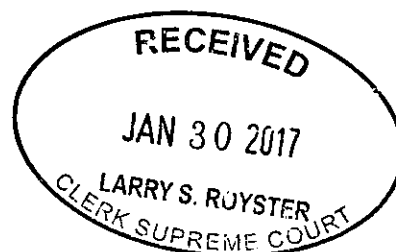
Dear Ms. Cavanagh:

Enclosed, please find a copy of our reply brief in the above referenced case. The reply was filed on January 30, 2017.

Very truly yours,



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Via Hand-Delivery

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Re: *Harmony Montessori Center v City of Oak Park; Reply Brief; Docket No. 154819*

Dear Clerk:

Please find enclosed Petitioner-Appellee's *Reply Brief In Support of Application for Leave to Appeal and Proof of Service* for the above reference case. Please time stamp copies of the *Reply Brief* and return to my courier.

If you have any questions regarding the enclosures, please contact me.

Very truly yours,

ALVIN L. STORRS LOW-INCOME TAXPAYER CLINIC


Joshua Wease

Enclosures

cc: Megan K. Cavanagh

